



THE PENINSULA

Against Expectations, U.S. and South Korean Growth Accelerates in the Third Quarter

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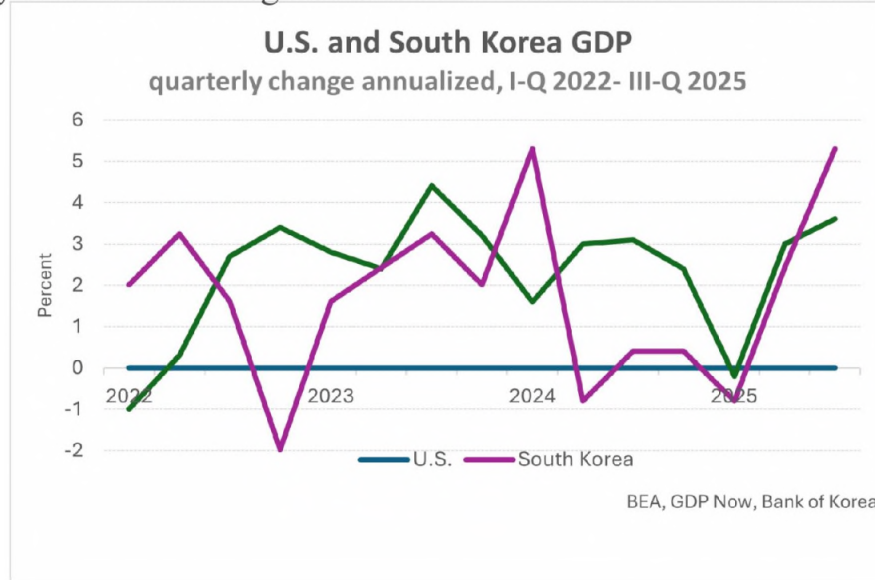
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The U.S. and South Korean economies continued to surprise forecasters in the third quarter with much better-than-expected growth. South Korea's GDP was very strong, growing at about a 5 percent seasonally adjusted annualized rate (SAAR) based on its revised estimate. Meanwhile, U.S. growth, not yet officially calculated due to the federal government shutdown delaying the data, 3.6 percent, according to analysis from the Federal Reserve Bank of Atlanta.

Both economies continued to accelerate from poor conditions early in the year, belying forecasts that had predicted slower growth or even recession given the tariff turbulence. The recovery has advanced South Korean GDP 1.7 percent above its third quarter 2024 level, while the United States is up about 2.6 percent, both above their recent trend of growth.



The similar results come from much different internal conditions. South Korea is a saver on its home turf and an investor abroad, while the United States is the opposite—a borrower from abroad and an investor at home. They are thus complements, and both are highly globalized, perhaps overly so. New governments in Seoul and Washington this year are attacking their long-running foreign dependency issues with some success, as seen in the third quarter. Seoul is trying to stimulate the economy by shifting to increased domestic demand, increasing government spending and pushing the large corporations to invest more at home while slightly lowering interest rates. The central bank is stymied, however, by a weak currency that would move even lower if it further eases.

South Korea Flips to Domestic-Led Growth

South Korea's third quarter GDP rose 1.3 percent over the previous quarter, according to the seasonally adjusted and not annualized measure preferred by the Bank of Korea. This represents a significant uptick in the quarter-to-quarter growth rate, up from 0.7 percent in the second quarter and a negative 0.2 percent in the first. Domestic demand provided almost all the growth, with the South Korean government pitching in about a quarter of the increased spending and giving tax inducements to spur private spending. GDP was also up 1.8 percent from the year-earlier quarter.

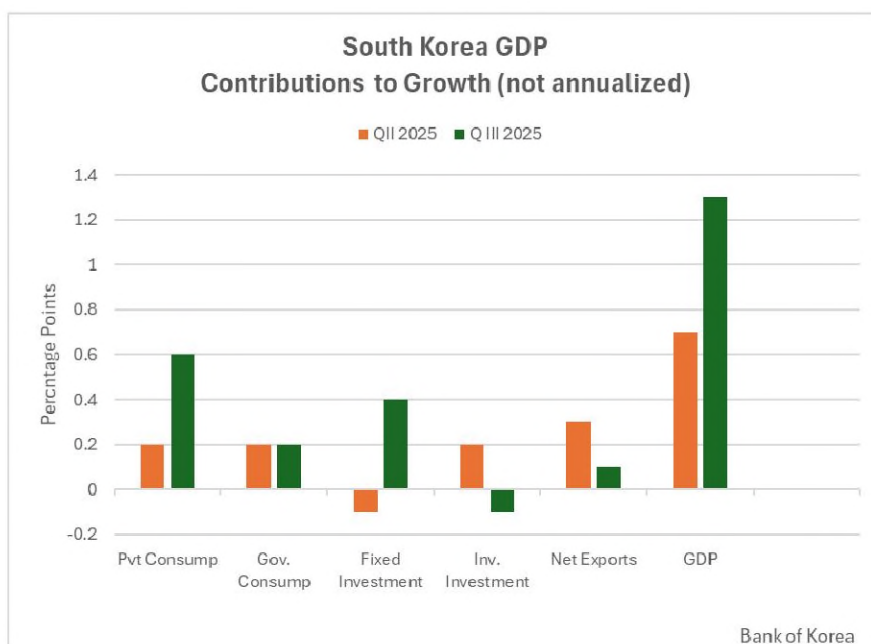
Surprisingly, private consumption jumped, adding 0.6 percentage points to GDP, or fully half of the overall growth. Government spending on consumption, largely health care, and public and private investment each added another 0.4 percent. Net exports added only a small 0.1 percent, as both exports and imports rose rapidly. The turnaround in investment, from a negative 0.1 percentage point decline in the second quarter to a positive 0.4 percent growth in the third, was a welcome change after little growth in previous quarters. New investment in the country's flagship chip industry, spurred by the worldwide boom in AI demand, led the way. Overall construction stayed flat and was far below year-earlier levels, an ongoing concern.

Exports of goods and services were surprisingly strong, largely due to semiconductor chips, contributing 0.7 percentage points to growth. But they were offset by a steep rise in imports that subtracted 0.6 percentage points. Trade remains highly volatile, with both major trade partners, China and the United States, facing structural issues. Weakness in the won/dollar exchange rate is likely protecting the export industry for the time being,

canceling out some of the disadvantages of the new U.S. tariffs and slowing Chinese demand. While the won is especially weak against the dollar, this year it is trending close to the yen and yuan.

South Korea's net foreign assets continued to rise in the third quarter by USD 27 billion, as the country spends its large current account surplus on foreign direct and portfolio investments. These purchases continue to put downward pressure on the won; the currency has fallen about five percent against the dollar in the past year, although it has held about even with the currencies of its other trade partners, especially Japan.

Since 2020, the won has reportedly lost 10 percent of its value against the weighted value of the currencies of its trade partners, as each are adjusted for inflation, despite continuing large surpluses on its current account. In effect, South Korea has been trading goods for foreign, and especially U.S., assets. This may be a permanent problem given the need of an aging population to securely save for retirement. It is like what happened in Japan in the 1990s, as its working age population began a sharp decline. In fact, the economies of Japan and South Korea are currently trending very close together.

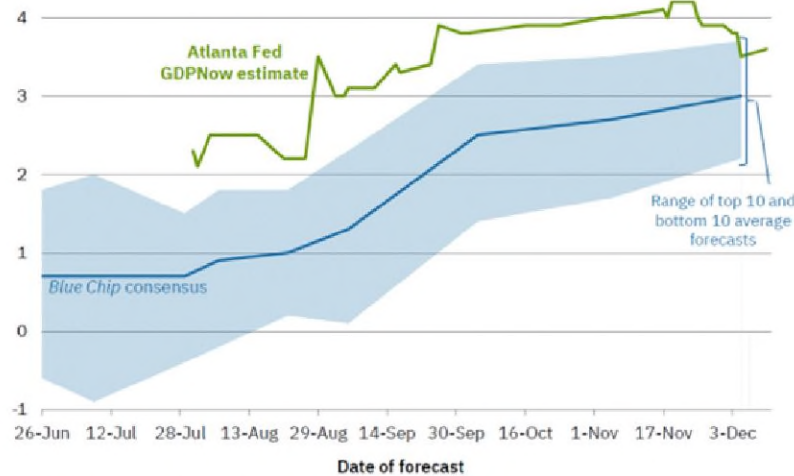


U.S. Data Delayed by Federal Shutdown, but Estimates Are Sharply Up

U.S. GDP is now widely expected to have continued its second quarter surge in the third quarter, according to the Wall Street Journal, surprising experts canvassed by the Blue Chip survey who in mid-summer expected 0.8 percent growth (see graphic below). The Bureau of Economic Analysis (BEA) canceled its third quarter advance estimate due to the federal shutdown and doesn't plan to release the preliminary estimate until December 23. In its place, economists are left with estimates such as those provided by The Federal Reserve Bank of Atlanta, a "nowcast" GDP proxy that includes actual released monthly data and interpolates gaps in as yet unreleased line items, which comes in at 3.5 percent as of early December. Early data on personal consumption and investment were both strong. It is not an official estimate but rather a modeled estimate of the current growth rate.

The nowcast, along with revised estimates, vividly show how the U.S. economy has defied several, more pessimistic forecasts from earlier this year; at the beginning of the quarter, not a few of the forecasts in the Blue Chip consensus, a regular survey of leading economists, expected a recession.

Evolution of Atlanta Fed GDPNow real GDP estimate for 2025: Q3
Quarterly percent change (SAAR)



Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts

Note: The top (bottom) 10 average forecast is an average of the highest (lowest) 10 forecasts in the Blue Chip survey.

GDP Estimates from the Atlanta Fed's "NowCast"

The estimates of faster growth come as the Donald Trump administration's tariffs are seen as having had much less impact on domestic output than had been expected—there has been little in the way of “retaliation”—or on inflationary pressure. While domestic demand has remained strong, at least through the third quarter, foreign suppliers have seemingly absorbed some of the tariff costs, and price increases have been restrained.

Mainstream estimates for the full year GDP suggest a substantial softening of fourth quarter GDP growth, harmed by slower demand for labor and slightly by the federal shutdown. Those costs can also be overestimated, however, by a flaw in the GDP measurement system, since federal payments to workers are added to GDP even if no work is performed. In fact, if workers found side jobs, GDP as measured would increase. Productivity of government work, not measured in the GDP process, was severely harmed, however.

Conclusion: Seoul Needs to be Wary of Japan's “Lost Decades”

As the United States sorts through its data and debt issues, causing consternation among its major trade partners, South Korea would do well not to rest on a few quarters of growth and concentrate on longer-term vulnerabilities. The country is still large dependent on foreign demand for its products, has a declining labor force, and still has a rather weak domestic investment. Encouraging better returns to capital at home to take advantage of Korea's large stock of savings and using these to support the aging population would appear to be a high priority. Record stock market prices in recent months suggest this may be occurring, and AI developments worldwide can help.

Foreign investors, however, continue to shy away from South Korea, possibly wary of the earlier political turmoil and the ongoing tensions with North Korea and China. The example of Japan, which fell into decades-long flat growth and a weakening yen, its savings flowing abroad rather than being reinvested in Japan much like Korea's current situation, is telling. Efforts to reverse this trend and bring in large amounts of U.S., Chinese, and Japanese stock investors would go a long way to boosting competition among South Korean industry, raising domestic South Korean investment and the won at the same time.

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